United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

75-7548

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

DOCKET NO. 75-7548

INTERNATIONAL CONTROLS CORP.,
Plaintiff-Appellee,

vs.

ROBERT L. VESCO, et al.,
Defendants,

and

VESCO & CO., INC.,
Defendant-Appellant.

CIVIL ACTION—ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK
SAT BELOW: HON. CHARLES E. STEWART, JR., U.S.D.J.

BRIEF FOR DEFENDANT-APPELLANT VESCO & CO., INC.

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STATEMENT OF ISSUES PRESENTED FOR REVIEW

1. Did the District Court err in failing to grant Vesco & Co., Inc. the right to be heard as to the merits of the claims against Robert L. Vesco?

2. Did the District Court err in ordering enforcement of a judgment which was neither valid nor final?

3. Was the District Court's finding that Vesco and Co., Inc. is the *alter ego* of Robert L. Vesco against the weight of the evidence?

4. Did the District Court err in ordering seizure of ICC stock owned by the Vesco children since 1966?

STATEMENT OF THE CASE

This is an appeal by defendant, Vesco & Co., Inc., (hereinafter referred to as "the Company"), from an Order entered under date of August 22, 1975 (1077a to 1083a) by the United States District Court for the Southern District of New York (Honorable Charles E. Stewart, Jr., presiding), finding that the Company is the *alter ego* of Robert L. Vesco, (hereinafter referred to as "Vesco") and determining that International Controls Corporation, (hereinafter referred to as "ICC"), is entitled to satisfy its judgments against Vesco by reaching shares of ICC stock owned by the Company.

Specifically, the Order mandated that a receiver be appointed to collect, from Vesco and the Company, all certificates of stock of ICC and Fairfield General Corporation in their possession within twenty days of such receiver's appointment; that Vesco apply for the required official consent for such transfer; and that the decision as to the right of ICC as judgment creditor, to seek cancellation of stock held by Vesco and the Company as judgment debtor(s), be deferred.

The captioned action [73 Civ. 2518 (CES)] was instituted on June 7, 1973. ICC filed a complaint (21a to 51a) against many defendants alleging numerous violations of the federal securities law, as well as other common law wrongs. The allegations centered around two general series of events, to wit: (1) certain transactions by those designated in the complaint as "Vesco and his group" and other alleged aiders and abettors regarding assets and funds of I.O.S. and other related companies; and (2) certain other transactions by the same personnae involving a Boeing 707 airplane.

Vesco & Co., Inc. is named in the caption of this action and appears for identification in paragraph 5 (r) (28a)

of the complaint, whereafter it is retired to the wings, receiving not so much as a mention in the body of the entire 27-page complaint. Preliminary injunctive relief was secured by ICC, and the Company and other defendants filed motions challenging such relief, jurisdiction and the sufficiency of the pleadings. See *ICC v. Vesco*, 470 F.2d 1334 (2 Cir. 1974). During the course of those proceedings, it was made clear that ICC would attempt to enforce against the Company any judgment it secured against Vesco, and, at all stages, the Company sought to preserve its rights to be heard on the merits and extent of any claims against other defendants.

On October 9, 1973, a default on the complaint was entered against Vesco (658a to 661a), which was eventually followed by a partial inquest setting damages at $2,422,466.72 (795a to 797a). However, following the default, but prior to the inquest, plaintiff filed an amended complaint (596a to 630a), adding new causes of action (some of them against Vesco) and joining additional defendants. The inquest purported to determine damages based upon the complaint which no longer existed, having been superseded by the amended complaint.

On April 8, 1974, ICC filed a complaint against Robert L. Vesco (74 Civ. 1588). Again a default was entered against Vesco, and the Company (not a named party therein) sought to intervene to be heard on the issues of liability and damages. The trial Court denied intervention (812a), assuring counsel that the Company would have its opportunity to be heard if ICC sought to satisfy its judgment against Vesco out of assets of the Company. The Company's appeal to the 2nd Circuit was denied, based, at least in part, upon the trial court's assurance that the Company would have its opportunity to be heard.

On May 20, 1975, ICC secured an order to show cause (822a to 842a), herein, in effect seeking to enforce

both of its default judgments against Vesco by securing assets of the Company. The Company responded by seeking a hearing on the merits of the underlying claims against Vesco, both as to liability and damages, and otherwise challenging the appropriateness of executing upon the judgments at that time (855a to 865a). The Court, apparently reversing its prior stated position that the Company would have the opportunity to be heard on the merits of the judgments sought to be enforced, denied the Company's applications and ordered a hearing only on the issues of whether the Company was the *alter ego* of Vesco or whether fraudulent conveyances had been made (822a to 825a).

The hearing was held on June 30, 1975. By memorandum decision dated August 22, 1975, the Court held that Vesco & Co., Inc. was the *alter ego* of Robert L. Vesco and that the assets of the Company were available to satisfy the judgments against Vesco as an individual (1077a to 1083a). The Court thus never reached the alleged issue as to whether fraudulent conveyances had been effected. Orders were entered (1098a to 1105a) which had the effect of securing shares of stock now owned by the Company, *without regard* to their prior ownership. Thus, stock owned by the Vesco children since approximately 1966 has been appropriated to satisfy the judgment against Robert L. Vesco, although no one has even alleged, much less proved, any impropriety by anyone dating back anywhere near said period.

In effect, the court below has granted plaintiff the right to have it both ways. While this defendant *is not* Robert L. Vesco for purposes of appealing the lack of procedural due process from service through judgment, and has not been permitted to be heard on the merits, it *is* Robert L. Vesco for purposes of enforcement. The actions of the court below were manifestly unjust and against the weight of the evidence.

Defendant filed its Notice of Appeal (1094a to 1097a) on September 19, 1975.

STATEMENT OF THE FACTS

Vesco & Co., Inc., ("the Company") is a Delaware corporation formed on July 12, 1972, an outgrowth of an estate planning technique conceived in late 1967 or early 1968 by counsel for the Vesco family in conjunction with its accountants.

Although such a plan was "in the works" for four years, its ultimate birth was occasioned by certain tax rulings received on April 26, 1972 (1292a to 1295a) and July 21, 1972 (1296a to 1298a).

The delay in implementation was explained by Vesco's accountant, Alan Bloom, at the order to show cause hearing on June 30, 1975 (1007a to 1012a). He detailed for the Court the necessity for an Internal Revenue Service ruling and the opposition of Hogan & Hartson, Vesco's securities counsel, to the program. Most importantly, Mr. Bloom pointed out that the ICC stock greatly appreciated in value and that the creation of the Company was not feasible and would not serve the function for which it was designed, if transfers occurred while the value was high. It was not until 1971 when the market price of ICC stock fell back to around $10.00 a share that the concept again became viable.

In the months of July through December of 1972, therefore, Vesco exchanged 800,000 shares of ICC common stock owned by him (having a value of $2,500,000) to Vesco & Co., Inc., in return for all of the preferred stock of the Company and a portion of the voting common stock. The preferred stock carried with it a liquidating preference equal to the same $2,500,000.

In addition, 46,380 shares of ICC common stock, beneficially owned by the Vesco children since 1966, was

exchanged for a minority of the voting common stock and all of the non-voting common stock of the Company.

The purpose and effect of the transfer was to put an upper limit on the value of Vesco's ICC holdings, for estate tax purposes, at the par value of the preferred stock (*i.e.* the appraised fair market value of that stock at the date of the exchanges), thereby permitting all future appreciation of that stock to inure to the benefit of the non-voting common shareholders—the Vesco children—and pass to them free of any estate tax.

Assets of the Company consist almost entirely of ICC stock. The Company's stock in turn, is *presently* owned as follows: The preferred stock is held by Vesco; all the common stock—the only voting stock—is owned by Patricia J. Vesco as custodian for her children.

Bloom further testified at the June 30, 1975, hearing that Mr. Vesco reactivated this estate planning device in 1971 (1002a) (not 1972), before the SEC investigation of ICC had passed its initial stages. The exhibits submitted, in particular the first Internal Revenue Service ruling request (1283a to 1288a) antedate the period covered by the testimony of Harry Sears, ICC's witness, clearly undercutting ICC's only attempt to show that the creation of Vesco & Co., Inc. was not motivated by legitimate tax considerations.

Significant in Mr. Sears' testimony were his statements that Robert L. Vesco was optimistic that he would prevail before the Securities Exchange Commission and that Vesco had received an opinion from Hogan & Hartson, eminent SEC practitioners, to the effect that the Commission did not have jurisdiction over the issues being investigated (967a to 968a). Additionally, as Mr. Sears' testified (968a), the thrust of the investigation was against

ICC, not Robert L. Vesco, and concerned the I.O.S. investment alone.

Notwithstanding this testimony of Vesco's accountant as to the legitimate purpose for the formation of the Company and notwithstanding the testimony of Harry Sears, ICC's own witness, that Vesco was advised by legal counsel that the SEC investigation was without foundation and that Vesco was optimistic during the relevant time period that the investigation would be dropped, the court concluded that Vesco & Co., Inc. was the *alter ego* of Robert L. Vesco, formed without a legitimate purpose, and a sham that should be disregarded. Considering the sparse proofs proffered by the plaintiff, it is clear that the Court was influenced by subsequent events not relevant to the issues presented and by the implicit assumption that Vesco was guilty of fraud, although there as no eviden presented to support such assumption.

Moreover, in orders implementing its *alter ego* decision, the Court, in effect, has directed seizure and/or cancellation of 46,380 shares of ICC stock beneficially owned by the Vesco children since approximately 1966. No showing was even attempted, much less made, that said stock was fraudulently conveyed to the children. However, unless this Court intervenes, the children's stock will be unjustifiably appropriated.

ARGUMENT

Point I

The District Court erred in failing to grant Vesco & Co., Inc. the right to be heard on the merits of the claims against Robert L. Vesco.

From the outset, the Company, despite numerous motions, comprehensive briefs and repeated protestations of the infringement of its rights, has been denied the opportunity to litigate the merits of plaintiff's claims against Vesco. The Company sought so to protect itself and its rights because it was openly and often stated in court that ICC would attempt to satisfy claims against Vesco by levying upon the assets of the Company (335a to 344a; 431a to 445a; 739a to 748a; 788a to 789a).

Nonetheless, the court below unabashedly has entered judgment against the Company, based upon prior judgments by default entered against Vesco, without permitting the Company the opportunity to challenge the procedural or substantive propriety of the underlying judgments. In effect, then, the Company has been subjected to massive judgments while simultaneously being foreclosed from contesting the merits of those judgments.

On May 22, 1974, when this matter came before the court below, upon partial inquest, counsel for the Company requested a hearing on the merits, and was rebuffed with this promise:

> "THE COURT: I think there may be reason to believe that you ought to have that full hearing. I would like to proceed this morning and I don't intend to require you to take positions today that you have not thought out and that you are not prepared to take because you have not developed a record.

"It seems to me we ought to proceed this morning and certainly I will give you full opportunity to be heard.

"I don't mean to suggest—I do mean to suggest, but I don't mean to reach any conclusion that by permitting you to participate at this stage that I have made up my mind in any respect as to the ultimate question of whether or not your client can be subjected to liability.

"I would like to indicate, as I have already done, that I think your participation in this hearing may not help your position on that matter" (743a-27 to 744a-10).

On July 12, 1974, as the partial inquest continued, the following dialogue took place between Mr. Laurence B. Orloff, representing the Company, and the Court:

"MR. ORLOFF: Your Honor, I should have an opportunity to put some evidence before the Court also, and I would most respectfully say that I should have the opportunity to put forth evidence, not only as to the dollar figure of any damage award, but also as to the liability issue.

"I realize that the plaintiff has taken a contrary position in its memorandum, but, as we suggested to your Honor in our memorandum, both from the standpoint of Vesco & Co.'s potential vulnerability for any judgment against Robert Vesco, and by virtue of the fact that there has been a conspiracy alleged among a number of defendants, who have not had a chance to defend themselves as yet, on this issue, no judgment should be entered until that defense is put in.

THE COURT: I have these thoughts about it:

It seems to me that in terms of the dollars, Mr. Carroll has told us what they are, and my notion is that this is reasonably clear.

> "On the other hand, what you say about the merits concerns me. I think I am obligated to give you a hearing on the question of conspiracy and on the merits. I'd like to do it promptly. What's your notion on it?
>
> "MR. ORLOFF: Within some reasonable time period, your Honor. I don't mean months, but I am talking certainly about several weeks. I would be ready on that" (779a-4 to 780a-5).

And later at that same hearing:

> "MR. ORLOFF: I was going to ask of Mr. Carroll through the Court whether I am therefore assured, and I guess I must respectfully ask the Court, too, that if a judgment were to be entered against Robert L. Vesco alone, would Vesco & Co. have an opportunity at a later date to be heard fully on the merits?
>
> "THE COURT: I have just been told by Mr. Carroll he doesn't want a judgment against Vesco & Co., Inc.
>
> "MR. ORLOFF: I think he is going to come in for one later on, and I want to make sure I will get my full hearing.
>
> "THE COURT: Of course you will" (789a-18 to 790a-5).

In another case entitled *ICC v. Vesco* (74 Civ. 1588), the Company was denied intervention, and judgment by default was taken against Vesco in the amount of $2,900,000. It is this judgment as well which plaintiff and the court below here intend to effectuate, by collection of the Company's assets.

In a hearing on that case held October 2, 1974, on the Company's motion to intervene, the following colloquy

took place between counsel for the Company and Judge Stewart:

> "THE COURT: So that it seems to me the question you are raising is in all respects premature.
>
> "MR. ORLOFF: If my client, Vesco & Co., has the right to challenge the existence of the cause of action at some point in time, if that is what your Honor means by premature, then I can see an [sic] accept your Honor's point. At the moment there is nobody raising that point. There is nobody pointing out to the court that there is no claim here really of corporate opportunity.
>
> "THE COURT: *Of course, the question will be presented to you if and when somebody comes after your client to try to get some of your assets, and then you will have full opportunity to litigate everything.* (emphasis added) (806a-21 to 807a-11).

A few moments later, the Court made the following pronouncement:

> THE COURT: . . . I would suppose it is possible that there might be a way to raise a claim that no cause of action was stated and that therefore you can't come after me. I don't think we have to worry about that at this point.
>
> It seems to me that the situation we are in today, Mr. Orloff and Mr. Camhy, is this: I am fully aware of the problems which are involved in this matter. I know who Vesco is. I know what Vesco & Co. is.
>
> Of course, you are not going to take the position that you are Vesco, which you aren't.
>
> And, of course, if Mr. Camhy reaches the point where he thinks he can go after Vesco & Co., Inc. to satisfy a judgment against Vesco, you are going to have the fullest opportunity to make whatever presentation you want. (811a-17 to 812a-9).

Despite these repeated assurances from the Court that the Company would have full and due opportunity to contest the merits of the underlying claims and related due process issues, the Court abruptly foreclosed the Company's rights and refused to consider any proofs on the legal propriety of the judgments now sought to be pressed as against the Company.

No longer is the Company's assertion of its right to be heard on the merits premature. Indeed, the propitious moment seems to have come and gone unheralded.

Memoranda submitted both before and after such "partial inquest" dealt squarely with that issue. In the Company's prehearing memorandum in the case *sub judice*, for instance, it argued that because of the unique nature of ICC's allegations that the Company is merely the *alter ego* of Robert L. Vesco, it should be entitled to contest any aspect of the liability asserted against him (710a to 722a).

The Company's present posture resembles that of a surety to whom a plaintiff turns, judgment in hand, for collection. But a surety stands in the shoes of its principal, and therefore, generally has the right to raise any defense which could have been asserted by that principal. For instance, in *Modern Brokerage Corp. v. Massachusetts Bond & Insurance Co.*, 54 F. Supp. 939 (S.D.N.Y. 1944), plaintiff sued the surety to recover on a performance bond for a construction project. The surety defended by raising plaintiff's refusal to enter arbitration proceedings, despite the principal's demand. Defendant, therefore, argued that the action should be stayed until the principal's right to compel arbitration was enforced.

The court in *Modern Brokerage* upheld this position, and more importantly, the surety's right to raise this, its principal's defense, because the "natural limit of the obliga-

tion of the surety is to be found in the obligation of the principal." 54 F. Supp. at 940. See also *United States v. Continental Casualty Co.*, 214 F. Supp. 949 (D.P.R. 1963); *Centraal Stikstof Verkoopkantoor, N.V. v. Alabama State Docks Dept.*, 415 F.2d 452 (5 Cir. 1969); *Association De Az. De Qua v. United States National Bank of Oregon*, 423 F.2d 638 (9 Cir. 1970).

Another situation graphically illustrates the Company's position vis-a-vis the court below. In *United States v. Borchardt*, 470 F.2d 257 (7 Cir. 1972), the government sought to foreclose a federal tax lien on certain property owned presently by defendant, Borchardt, but previously by defendant, Mensik. When Mensik defaulted, the United States asserted that Borchardt could not allege Mensik's defenses, to wit: the running of the statute of limitations and fraudulently induced waivers of limitations.

The Court, rejecting the government's position, allowed Borchardt, as grantee of the property in question, to assert such defenses, despite the Mensik default. See also, *Hawkeye-Security Ins. Co. v. Schulte*, 302 F.2d 174 (7 Cir. 1962).

In such cases, the defense belonging to the defaulting party was permitted to the party against whom judgment would be enforced. Such too should have been the case here for the Company. The court below, having placed it squarely "in the shoes" of Robert L. Vesco for purposes of its remedy against him, should have permitted the Company to stand in those shoes for purposes of rebutting the merits of the claim. Its holding to the contrary is a denial of the Company's fundamental due process rights, and an abuse of the Court's discretion.

For, indeed, ICC has never proved its right to prevail. The court below has permitted ICC to avoid totally its

liability proofs. The Company, which has appeared, which has not defaulted, and which has continuously pressed to rebut the merits of ICC's case, must be permitted to test the allegations of the pleadings in an adversary hearing.

While the Company was given the right at the show cause hearing on June 30, 1975, to speak to the *alter ego* issue, it was expressly denied the opportunity to address the claims themselves *on its own behalf*. For instance, as stated in counsel's post-hearing memorandum:

> "The judgment which has been entered in this case concerns charges for an airplane which were not liabilities, in fact, for the most part, had not been incurred by the time of the creation of Vesco & Co." (1046a-12 to 15).

The truth *vel non* of this statement was somehow judged to be irrelevant in the face of Vesco's default.

Trans World Airlines, Inc. v. Hughes, 449 F.2d 51 (2 Cir. 1971) was a case cited below by ICC to buttress the concept that by default a defendant admits every "well pleaded allegation" of the complaint. *Thomson v. Wooster*, 114 U.S. 104, 29 L.Ed. 105 (1885).

The Circuit Court was reversed and remanded in *Hughes Tool Co. v. Trans World Airlines*, 409 U.S. 363, 93 S. Ct. 647, 34 L.Ed.2d 577 (1973) *reh. den.* 410 U.S. 975, 93 S. Ct. 1434, 35 L.Ed. 2d 707 (1973). Despite a default judgment taken in the amount of over $145,000,000, the Supreme Court rang down the curtain on that protracted litigation with directions to the District Court to dismiss the complaint as a matter of law. Therein, the Supreme Court heard, considered, and ruled upon (favorably to the defaulting party) the underlying legal issues, without regard to the fact that judgments had been entered by default.

Herein, the situation is all the more compelling. The court below has, in effect, saddled the Company with the default judgment of another party, while expressly denying the Company the right to delve into whether the underlying default judgments were legally meritorious or procedurally proper. This decision is not only contrary to the "law of the case," as repeatedly articulated in prior statements made by the court in this and related proceedings, but is a shocking denial of the fundamental concepts of due process of law. In short, the Company has been found subject to judgments of upwards of $5,000,000 and yet been refused the right to question the lawfulness of these judgments.

Point II

If the Court determines the Company has a right to be heard on the merits of ICC's claim against Vesco, it must also consider fundamental due process issues.

From the outset, the Company has vigorously contended that Robert L. Vesco has been treated in a manner inconsistent with all notions of fundamental due process.

In a letter addressed to the Honorable Charles E. Stewart, dated July 9, 1973, counsel for the Company stated:

> "I respectfully suggest to Your Honor that the above-detailed series of events would seem to abrogate accepted standards of fair play and due process of law. Established common law, statutory, and constitutional principles of due process have seemingly been abandoned in this case amidst the large number of charges hurled at the various defendants by plaintiff, ICC. When I indicated previously that this proceeding threatened to take on all of the earmarks of a unilateral investigatory rather than a

> judicial proceeding, I was hopeful that its direction would change. The above course of events have demonstrated, I fear, (and I say this with full respect and consideration for the Court and its processes) that our most dire apprehensions have been realized" (543a-22 to 544a-10).

Such a pattern of due process denial has, reflective of the court's *alter ego* findings and their ultimate result, culminated in a parallel due process denial for the Company. If Vesco & Co., Inc. is to be clothed with standing to defend this case on its merits, the Court must also consider these basic substantive and procedural defects.

A. *The manner of service failed to secure personal jurisdiction over Robert L. Vesco*

Service of process upon the defendant, Robert L. Vesco in this action was ostensibly effected by Lois S. Yohonn ("Yohonn"), an attorney associated with the plaintiff firm, Shea, Gould, Climenko, Kramer & Casey in New York, as authorized by two court orders issued by Judge Charles E. Stewart, United States District Court, Southern District of New York.

The first order, dated July 27, 1973 (a Friday) (568a to 569a), permitted her merely to serve that defendant, reciting simply that she was so qualified and that speed was essential. The manner of service was not specified nor were there any asserted facts to support the contention that speed was essential.

Acting upon such order, Yohonn went to Nassau, the Bahamas on Saturday, July 28, 1973, where, according to her affidavit, she tried in vain to serve Vesco personally. Hearing that a house on Brace Ridge Road, where he allegedly was living, was protected by guards, she did not

at first attempt service there, but instead, according to her affidavit (577a to 583a), spent Sunday and Monday, July 29 and 30, seeking Vesco out in places he was rumored to frequent.

When, late in the afternoon of July 30, she finally arrived at the Brace Ridge Road address, Yohonn was, indeed, denied access to the house. Instead, she threw the papers at a teenaged boy who, she believed, was Vesco's son. He threw them back to her. Nothing in her affidavit indicates the presence of Vesco at Brace Ridge Road at that time.

Upon returning to her hotel room, Yohonn alleges, she telephoned Judge Stewart at his chambers in New York, requesting that he authorize her to use an ancillary order previously prepared and signed in New York on Sunday, July 29, 1973 (570a to 571a). Her request was summarily granted.

Such order stated that service of process upon Robert L. Vesco "may be effected by depositing a copy of the papers upon the premises of that last known residence of the defendant located in Nassau, Bahamas," and by mailing a copy to that defendant at the same address.

Returning to Brace Ridge Road, Yohonn rolled up the papers, tied them with a blue ribbon, and tossed them over a wall onto the lawn a few feet from the front door to a house. She then photographed the premises with the papers lying upon the lawn. Guards followed her back to her cab, demanding that she take back the papers. "Service" thus effected, Yohonn directed the driver to take her from the scene.

Such service failed to comport with fundamental notions of due process and notice which must be satisfied before a court can obtain personal jurisdiction.

The principal question which a court must raise when sufficiency of service is attacked on such due process

grounds, is whether process was served in a manner "reasonably calculated to give a party actual notice of proceedings against him." *Hoffman Motors Corp. v. Alfa Romeo, S.P.A.*, 244 F. Supp. 70 (S.D.N.Y. 1965); *Millikin v. Meyer*, 311 U.S. 457, 61 S. Ct. 339, 85 L. Ed. 278 (1940); *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 70 S. Ct. 652, 94 L. Ed. 685 (1950).

Measured against this standard, it cannot seriously be argued that tossing a summons and complaint upon what are merely assumed to be the last known premises of Vesco, was a method "reasonably calculated to give actual notice" of the proceedings to Vesco. Following this with service by ordinary mail to these same premises added little to plaintiff's efforts.

Case law has applied the concepts of due process to numerous situations where the customary method of performing personal service was eschewed. In *Clover v. Urban*, 142 A. 389, 108 Conn. 40 (Sup. Ct. of Errors, Conn. 1928), for instance, a default judgment was held void and of no effect where the summons and complaint were left in the outer hall of a two-family dwelling rather than within defendant's own place of residence. The Court stated that the "usual place of abode" requirement ensures actual notice; therefore, leaving the papers in an outer hall used commonly by two tenants fails "just as completely as if it had been left on a common sidewalk or common yard." *Id.* at 390.

Was service in Nassau itself "reasonably calculated to ensure actual notice?"

Because of the notoriety accompanying his every movement, and the wide press coverage Vesco was receiving, both plaintiff and the court below knew, or should have known, that his "last known residence" was, in fact, Costa Rica. Indeed, an affidavit on June 18, 1973 (over

a month earlier), by special counsel David Butowsky, characterizes Vesco as a "fugitive from justice residing in *Costa Rica*." (emphasis added) (321a-17).

The Company submits that service in Nassau was calculated to appear to meet due process standards, while denying Vesco lawful notice of the proceedings. There appears to be no valid reason, moreover, why service, if it was to be effected in Nassau, could not have been entrusted to the relevant government authorities of the Bahamas.

Fed. R. Civ. P. 4(i) governs service in a foreign country. Although it is true that *Rule* 4(i)(1)(E) provides for service as directed by order of the Court, it is likewise true that any departure from the provisions whereby service is effected otherwise than by delivering a copy of the summons and complaint to the defendant in person is subject to constitutional notions of due process. 2 Moore's *Federal Practice* §4.09, p. 1028.

A defendant has been deemed entitled either to service upon himself personally or to service in substantial compliance with the rule, *Id.* at §4.11[2], courts being "without authority to nullify the plain requirements of the rule providing how jurisdiction may be acquired over the person of defendant." *Zuckerman v. McCulley*, 7 F.R.D. 739 (E.D. Mo. 1947).

The Yohonn affidavit demonstrates that personal service upon Vesco was only cursorily attempted before the peremptory issuance of an order by Judge Stewart via international telephone, allowing Yohonn to serve process as she would a tennis ball.

As a matter of due process, such acts fail to "substantially comply" with personal service requirements. Plaintiff made no attempt whatever to assure that the summons

and complaint were delivered to a responsible party acting on behalf of the defendant or to a place where defendant would be assured of receiving them.

Therefore, service pursuant to the July 27 and 29, 1973 orders should be held insufficient to give personal jurisdiction over defendant Robert L. Vesco.

B. *Service of Process Pursuant to a Sunday order is invalid*

The unanswered summons and complaint upon which a default was taken against Robert L. Vesco were "served" pursuant to an order signed by the court below on Sunday, July 29.

Such a judicial act is void according to the general common law rule and statutory enactments in many jurisdictions. Annot. "Judgment on Sunday or Holiday," 85 *A.L.R.* 2d, p. 595 (1962); 83 *C.J.S., Sunday*, §53, p. 379 (1953). The common law rule is expressed by the Latin phrase, "dies dominicus non est dies juridicus," (God's day is not a judicial day). 85 *A.L.R.* 2d, at 596. See also *Stone v. United States*, 64 F. 667 (9 Cir. 1894); *Dayton Power and Light Co. v. Federal Power Commission*, 251 F.2d 875 (D.C.C.A. 1957); *District of Columbia v. General Federation, etc.*, 249 F.2d 503, 504 (D.C.C.A. 1957).

To date, no reported federal decision has been found which deals specifically with the efficacy of a Sunday order, as opposed to another judicial act such as a judgment or receipt of a verdict. Unlike the federal courts, however, the courts of the State of New York have repeatedly addressed the validity of judicial acts and proceedings performed on Sunday.* New York Judiciary Law §5, a substantial enact-

* Under *Erie R.C. v. Tompkins*, 304 U.S. 64, 58 S. Ct. 817, 82 L.Ed. 1188 (1937), the substantive law of the State of New York would be applicable to this proceeding.

ment of the common law rule (see *Jones v. East Meadow Fire District*, 249 N.Y.S. 2d 771, 21 A.D.2d 129 (App. Div. 1964), provides as follows:

> §5. Courts not to sit on Sunday except in special cases.
>
> A court shall not be opened, or transact any business on Sunday, except to receive a verdict or discharge a jury and for the receipt by the criminal court of the City of New York or a Court of Special Sessions of a plea of guilty and the pronouncement of sentence thereon in any case in which such court has jurisdiction. An adjournment of a court on Saturday, unless made after a cause has been committed to a jury, must be to some other day than Sunday. But this section does not prevent the exercise of the jurisdiction of a magistrate, when it is necessary to preserve the peace, or, in a criminal case, to arrest, commit or discharge a person charged with an offense, or the granting of an injunction order by a justice of the supreme court when in his judgment it is necessary to prevent irremediable injury or the *service of a summons with or without a complaint if accompanied by an injunction order and an order of such justice permitting service on such day.* L. 1909, c.35; amended L.1930, c.602; L.1962, c.698, §31, eff. Sept. 1, 1962 (emphasis added).

Judge Stewart's Sunday order in the instant case was not grounded upon or accompanied by an injunction order; and that section is the only even colorable exception to the Sunday proscription against *court business.*

That the order was "court business" is clear. Plaintiff ostensibly obtained the order allowing service pursuant to *Fed. R. Civ. P.* 4(i)(1)(E), which provides that a party may be authorized to serve process in a foreign country in a manner "as directed by order of the Court."

The language of that Rule is crucial here because New York courts distinguish, for purposes of the Sunday ban, between judicial business which can be done by a justice out of court and judicial acts which require application to a court. It is beyond question that *Rule* 4(i)(1)(E) requires application to a court.

Thus, while it has been held that a judge may, for instance, properly grant an order to show cause *acting out of court* on a Sunday, such an order does not require application to a court. Indeed, there is specific authority under the New York Civil Practice Act §65, that a justice may, at reasonable times, transact certain judicial business which may properly be done *out of court*. See *Banko v. Weber*, 192 N.Y.S.2d 260, 9 A.D.2d 732 (App. Div. 1959), *aff'd* 7 N.Y.2d 758, 193 N.Y.S.2d 670, 162 N.E.2d 750 (1959). But where the performance of a judicial act requires application to a court, such application cannot be made to a judge except in court. *Aiken v. Aiken*, 160 N.Y.S. 876, 96 Misc. 561 (Sup. Ct. Monroe Cty. 1916).

Although Section 452 of Title 28 of the United States Code states that "all courts of the United States shall be deemed always open for the purpose of filing proper papers, issuing and returning process, and making motion and orders, . . .", there is, to date, no authority for the proposition that this Section overrules either the common law or statutory rule in effect in New York.

Since the enactment of that federal statute, counsel for the Company has found it cited on this issue only once, in a case which supports the proposition that 28 *U.S.C.* 452 cannot and does not supersede local substantive law. In *Williams v. National Surety Corp.*, 153 F. Supp. 540 (D.C. Ala. 1957), *aff'd* 257 F.2d 771 (5 Cir. 1958), a federal jury returned a verdict on a Sunday. The court refused reliance upon the federal statute, analyzing instead the com-

mon and statutory law of Alabama to conclude that, under Alabama law, the receipt of a jury verdict on Sunday was permissible. Similarly, under the state law here in question, the signing of the order concerned herein was not permissible.

Because Judge Stewart's order signed on July 29, 1973, is void, it follows that service of process based thereon is invalid and of no effect.

C. *Judgment against Vesco is not enforceable because plaintiff filed an amended complaint after default was entered*

The original complaint in this action below was filed on June 7, 1973. Service upon Vesco was allegedly effected on July 30, 1973, and default judgment entered on October 5, 1973.

Such judgment, while it did not designate the amount of Vesco's liability, provided for an inquest to determine that amount. Clearly, the damages must reflect the allegations of the complaint.

However, on September 7, 1973, plaintiff filed an amended complaint and again attempted service of process upon Vesco. The amended complaint, *inter alia*, added to the number of parties-defendant and raised additional claims for damages against the defendants, including Vesco.

Then on July 12, 1974, judgment was filed in the Court against Vesco (795a to 797a) in the amount of $2,422,-466.72, ostensibly based on the October 5, 1973, default judgment. It was recited that the cause had been brought before the Court for partial inquest on May 14, 22 and July 12, 1974; that the required notice was given to Vesco; and ordered that plaintiff have execution for the amount of the

judgment, and the right to prove additional losses by reason of the acts alleged in "*the complaint*" (796a-14). The judgment did not state whether the recovery was based only upon the amount sought in the original complaint or upon the increased damages sought in the amended complaint.

According to 3 Moore's *Federal Practice* §15.08[7], an amended pleading that is complete in itself and makes no reference to nor adopts any portion of the prior pleading, supersedes it. *Nisbet v. Van Tuye*, 224 F.2d 66 (7 Cir. 1955); 71 *C.J.S., Pleading*, §321 (1951). Thus, it has been held a matter of "hornbook law that an amended complaint, complete in itself" renders a prior complaint "functus officio," of no legal effect and no longer functioning. *Lubin v. Chicago Title and Trust Co.*, 260 F.2d 411 (9 Cir. 1956).

This rule was the basis, for example, of the holding that a judgment cannot be rendered in favor of a party who was named in a first complaint but not in a superseding amended complaint because the original complaint no longer functions as a pleading. *Bullen v. De Bretteville*, 239 F.2d 824 (9 Cir. 1956), *cert. den. sub nom. Treasure Co. v. Bullen*, 353 U.S. 947, 77 S. Ct. 824, 1 L.Ed.2d 856; *Ciccetti v. Lucy*, 514 F.2d 362 (1 Cir. 1975).

Further, it has been stated that a default judgment may be vacated *in effect*, albeit not formally set aside, by subsequent proceedings in the same action which are inconsistent with it. 49 *C.J.S., Judgments*, §338 (1947), *Freeman on Judgments* (5th Ed. 1925) §1278. For instance, in *Clarke v. Higdon*, 81 A.2d 650 (D.C. Mun. Ct. 1951), defendant in default on an original complaint which sought damages of $450, was found to be no longer in default when complaint was amended, seeking judgment for $550; defendant was held entitled to an opportunity to plead and defend on the amended complaint.

Common sense and due process standards dictate that where, as herein, an original complaint is abandoned in favor of an amended complaint, the amended complaint replaces it and renders it nonfunctional for all purposes relevant to the proceedings below. A court would, therefore, lose its power to proceed on the original complaint; thus the default judgment based upon failure to plead to the first complaint is of no effect. Enforcement against the Company must, as a matter of law, also fail.

° ° °

For these reasons, and others expressed by the Company throughout these complex proceedings, it is respectfully submitted that this Court cannot and should not avoid, as did the court below, full and plenary disposition on these fundamental issues, sought, fruitlessly, to be adjudicated by this defendant.

Point III

The judgment entered against Robert L. Vesco is not final, and, therefore, cannot be the subject of execution.

A. *A court cannot render final a partial adjudication of the interests of a party*

The judgment by default against Vesco filed with the court below on October 5, 1973, stated, in relevant portion, that ". . . there is no just reason for delay in entering the within judgment against defendant Robert L. Vesco" (659a-15), and ordered that judgment be entered for ICC against him, granting injunctive and declaratory relief.

The order did not designate the amount of Vesco's liability, but further provided for an inquest to determine

the amount of liability; upon the completion of that inquest, the judgment would be amended to a specific dollar (or in this case, multi-million dollar) figure. This amended judgment, it was provided, could be entered against Vesco alone.

When, on July 12, 1974, the amended judgment (795a to 797a) was filed in the District Court against Vesco, total damages were computed as $2,422,466.72. The judgment further recited that the required notice had been given, and ordered that plaintiff have execution for the amount of judgment, reserving the right to prove additional losses by reason of the acts alleged in the complaint.

The second judgment stated neither that it was a "final" judgment nor an amended judgment.* Nevertheless, with judgment in hand, plaintiff pursued its prey. The Company was found to be the *alter ego* of Vesco, and ordered to turn over its assets to a newly appointed receiver.

It is important at the outset that the terms "final" and "interlocutory" judgments be distinguished from each other; under the Federal Rules of Civil Procedure, the term "judgment" is sufficiently broad to encompass all interlocutory or provisional orders or decrees which are appealable, as well as all "final" judgments. *Fed. R. Civ. P.* 54(a). See 6 Moore *Federal Practice*, §54.02 (2 Ed. 1974). But a final decision must be "one which ends the litigation . . . and leaves nothing for the court to do but execute judgment." *Catlin v. United States*, 324 U.S. 229, 65 S. Ct. 631, 89 L. Ed. 911 (1945).

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* A new order filed on September 11, 1975 (1091a to 1093a), *ex parte* declared *ipse dixit* that such judgment was and is final and that no further action of any court is required for execution of that judgment. As in the previous judgments, plaintiff was given the right to prove and recover other amounts pursuant to the October 5, 1973, default judgment.

Both the first and second judgments contain a provision which permits the plaintiff to prove additional damages or losses suffered by reason of the acts alleged in the complaint.

Judgment in favor of the plaintiff but without a determination as to the amount of damages suffered is *not* a final judgment. *Western Geophysical Co. of America, Inc. v. Bolt Associates, Inc.*, 463 F.2d 101 (2 Cir. 1972), *cert. den.* 409 U.S. 1040, 93 S. Ct. 523, 34 L. Ed. 2d 489 (1972). It accordingly follows that the first judgment filed October 5, 1973, was not—despite the certification by the District Court—a final judgment, since it lacked a determination as to the amount of damages; the court moreover abused its discretion by making such a certification. See *Sears, Roebuck & Co. v. Mackey*, 351 U.S. 427, 76 S. Ct. 895, 100 L. Ed. 1297 (1956).

Although the subsequent judgment filed July 12, 1974, did specify an amount of damages, this latter judgment also is defective. First, the judgment expressly provides for possible modification and reopening of the amount of damages, and thus the finality of the judgment is manifestly questionable. Second, the latter judgment does not include the mandatory certification of the District Court under *Rule* 54(b) that there is "no just reason for delay." Without such a certification and without any provision declaring that it is an amended judgment of the October 5, 1973, judgment, the latter judgment violates *Fed R. Civ. P.* 54(b).

B. *The judgment against Vesco is not final because he was one of multiple defendants against whom joint liability is alleged*

The complaint in this action upon which default judgment against Vesco is based, alleges, in part, that he, in

conspiracy with certain other named defendants, committed acts in violation of the federal securities laws, and in breach of fiduciary obligations to ICC; this raises the specter of joint liability among all those defendants. See Harper & James, *Law of Torts*, §10.1, 10.2 (1956).

The Company is informed that actions against most of Vesco's co-defendants remain pending in the court below; neither judgments nor dismissals have yet been entered as to them.

It is, of course, true that *Fed. R. Civ. P.* 54(b), as amended in 1961, provides that, when multiple claims or parties are involved in an action, a final judgment may be entered "as to one or more but fewer than all of the claims or parties."

However, where there are several defendants, alleged to be jointly liable, it is generally held that entry of a default judgment against one defendant cannot be made until all the defendants are in default or the case is tried as to the defendants not in default. In *Frow v. De La Vega*, 82 U.S. (15 Wall.) 552, 554, 21 L. Ed. 60 (1872), the Supreme Court of the United States said:

> "The question is, whether the court, in such case as this, could lawfully make a final decree against one defendant separately on the merits, whilst the cause was proceeding undetermined against the others. If it could be done, then this absurdity might follow: there might be one decree of the court sustaining the charge of joint fraud committed by the defendants, and another decree disaffirming the said charge, declaring it to be entirely unfounded and dismissing the complainant's bill. And such an incongruity, it seems, did actually occur in this case. For, after this final decree against the appellant, the Court proceeded to try the issues made by the answers of the other defendants, and decided the merits of the cause

adversely to the complainant, and dismissed his bill. This fact is made to appear by the return to a certiorari sued out by the appellee himself.

"Such a state of things is unseemly and absurd, as well as unauthorized by law.

"The true mode of proceeding where a bill makes a joint charge against several defendants, and one of them makes default, is simply to enter a default and a formal decree pro confesso against him, and proceed with the cause upon the answers of the other defendants. The defaulting defendant has merely lost his standing in court. He will not be entitled to service of notices in the cause, nor to appear in it in any way. He can adduce no evidence; he cannot be heard at the final hearing. But if the suit should be decided against the complainant on the merits, the bill will be dismissed as to all the defendants alike—the defaulter as well as the others."

In *United States v. Peerless Insurance Company*, 374 F.2d 942 (4 Cir. 1967), a case decided five years after the amendment of *Fed. R. Civ. P.* 54(b), the Court discussed the case of *Frow v. De La Vega, supra*, and concluded that it remains the law. As the court stated:

"Although *Frow* was a case of joint liability, we think the procedure established for multiple defendants by Rule 54(b) is strikingly similar and applicable not only to situations of joint liability but to those where the liability is joint and/or several. Such an interpretation finds some support in the common law: 'there may be entered an interlocutory judgment of default against the defaulting defendant, but a final judgment cannot be entered on the default until the issue as to the other defendants is successfully disposed of.' 49 C.J.S. Judgments §191(b)(2), at 329 (1947). Even under statutes permitting separate judgments it has been held that a default judgment

> may not 'be entered against a defendant who is only secondarily liable, until a successful termination of the suit against defendant primarily liable.' Id. at 330.
>
> "In Moore, Federal Practice, it has been said: '[W]here the liability is joint and several or closely interrelated and a defending party establishes that plaintiff has no cause of action or present right of recovery, this defense generally inures also to the benefit of a defaulting defendant,' citing *American Coat Pad Co. of Baltimore City v. Phoenix Coat Pad Co.*, 113 F. 629, 633 (4th Cir. 1902),) and other decisions. 6 Moore Federal Practice §55.06, at 1821 (2d ed. 1965)." 374 F.2d at pages 944-945.

Simply denominating a partial adjudication as "final" will not make it so. *Sears, Roebuck & Co. v. Mackey, supra.* Indeed, in *Robbin v. American University*, 310 F.2d 225 (D.C. Cir. 1964), it was held an abuse of discretion for the court to act under *Fed. R. Civ. P.* 54(b) to dismiss a complaint against one party and order the entry of final judgment where the appeal of the dismissal might possibly affect the adjudication of the claims pending against the remaining defendants at the trial level. Such a ban mirrors the *Frow* prohibition. Clearly, the law will not authorize the entry of a final judgment against a defaulting defendant where there is a joint complaint against several defendants and a possibility that the litigation against the remaining defendants on the merits will produce a result that will inure to the benefit of the defaulting party.

Even if the October 5, 1973, July 12, 1974, and September 11, 1975, pleadings signed by Judge Stewart purport to be final judgments by containing the specific language required by *Fed. R. Civ. P.* 54(b), the mere inclusion of those words, cannot render final a decision which is not final. Such a judgment cannot be prematurely executed upon, absent a determination of the issue of joint liability.

The theory of joint liability belongs to the plaintiff. The court below must ensure that it is proved or disproved as to the alleged conspirators before the default disposition can be afforded finality, and the plaintiff awarded execution.

Thus, if joint liability is subsequently decided against the plaintiff on the merits, the complaint should be dismissed as to all of the defendants, both those who have appeared and those who have defaulted. See *Frow v. De La Vega. supra; Overfield v. Pennroad Corp.*, 42 F. Supp. 586 (E.D. Pa. 1941); 6 Moore, *Federal Practice, supra,* §55.06. As applied to the present situation, the default judgment entered against Mr. Vesco would not appear to be a final judgment, despite the certification of finality issued by the District Court in the judgment filed October 5, 1973, and July 12, 1974, and the order of September 11, 1975, since the action remains pending against the other defendants and no proof has yet been introduced on the *merits* of the plaintiff's allegations, against either Vesco or his co-defendants.

° ° °

For the reasons described above, the judgments entered as against Robert Vesco are not "final," both because of the procedural and formal defects and because of the joint nature of the claims herein. Accordingly, these judgments cannot and should not be the subject of interlocutory execution. *Sears, Roebuck & Co. v. Mackey, supra,* at 435-437; *Dickenson v. Petroleum Corp.*, 338 U.S. 507, 511-512, 70 S. Ct. 322, 94 L. Ed. 299 (1950); *Redding & Co. v. Russwine Const. Corp.*, 417 F.2d 721, 135 U.S. App. D.C. 153 (D.C.C.A. 1969); 6 Moore, *Federal Practice* §54.27 (2d Ed. 1963), §54.42, ¶273-74 (2d Ed. 1963); 49 *C.J.S., Judgments* §586(a) (1947); 33 *C.J.S., Executions* §6.

Point IV

The finding that the Company is the *alter ego* of Vesco is against the weight of the evidence and is unsupportable under applicable law.

On June 30, 1975, the court below convened on order to show cause why ICC is not entitled to satisfy its judgments against Vesco by execution upon assets of the Company. Two judgments were involved: one, in the instant case, in the amount of $2,422,466.72 (73 Civ. 2518 [CES]); the other, in the amount of $2,900,000.00 in *ICC v. Vesco*, 74 Civ. 1588.

Both judgments had been taken by default; for purposes of both judgments, ICC alleged and the court found that the Company was a sham to be disregarded, the *alter ego* of Vesco. On that theory, the court ordered seizure of the Company's assets to satisfy both judgments.

The first questions to be addressed are what, as a matter of law, did ICC have to prove in order to pierce the corporate shield? What quantum of proof was necessary?

The doctrine that a corporation may be disregarded when it is the mere *alter ego* or business conduit of a person has been stated in general terms as follows:

> ". . . The theory of alter ego has been adopted by the courts in those cases where the idea of the corporate entity has been used as a subterfuge and to observe it would work an injustice. To establish the alter ego doctrine it must be shown that the stockholders' disregard of the corporate entity made it a mere instrumentality for the transaction of their own affairs; that there is such unity of interest and ownership that the separate personalities of the corporation and the owners no longer exist; and to adhere to the doctrine of corporate entity would promote injustice

> or protect fraud." I Fletcher *Cyclopedia Corporations*, §41.2, Permanent Edition (1963).

ICC, then, had to prove that the Company was formed and utilized as no more than a subterfuge, to promote injustice and protect fraud.

Additionally, the power to disregard the corporate entity is only to be exercised in most exceptional circumstances. In *Zubik v. Zubik*, 384 F.2d 267 (3 Cir. 1967), the Court issued the following admonition as to the exercise of that power:

> "In applying the test, however, any court must start from the general rule that the corporate entity should be recognized and upheld, usless specific, unusual circumstances call for an exception . . . Care should be taken on all occasions to avoid making the entire theory of the corporate entity . . . useless. . . .
>
> "Limiting one's personal liability is a traditional reason for a corporation. Unless done deliberately, with specific intent to escape liability for a specific tort or class of torts, the cause of justice does not require disregarding the corporate entity" 384 F.2d at p. 273.

It was also emphasized in *Zubik* that parties wishing to prove that the corporate entity should be disregarded have the burden of establishing *by a preponderance of the evidence* that the "corporation was an artifice and a sham designed to execute illegitimate purposes in abuse of the corporate fiction and the immunity that it carries." *Id.*, at p. 270. In the case of *In Re Chas. K. Horton*, 22 F. Supp. 905 (S.D. Tex. 1938), the Court vigorously supported the notion that the quantum of proof required to disregard the corporate form is great and that every reasonable presumption is indulged in favor of the corporate body:

> ". . . Courts exercise great caution in ignoring the artificial entity, and such ignoring only comes if and when the proof substantiates the thought, and drives any other conclusion from the mind, that the entity is in fact the tool or mere agency of the owner of the stock" (citations omitted) *Id.* at p. 908.

Professor Fletcher's comment as to the determination of the question is that:

> ". . . a mere allegation that a coporation is the alter ego of individual stockholder[s] is insufficient in the absence of allegations of facts from which it will appear, *and the presumptions are that the stockholders or officers and the corporations are distinct entities*" (emphasis added).
>
> 1 Fletcher *Cyclopedia Corporations*, §41.3, Permanent Edition (1963).

Thus, in applying the above test in the context of litigation where a claimant seeks to disregard the corporate form, the federal courts have repeatedly held, presumably because of the high burden placed on the claimant, that the mere fact of sole ownership and control of all or substantially all the corporate stock, is insufficient to establish the *alter ego* relationship. See *e.g.*, *Delta Theatres v. Paramount Pictures*, 259 F.2d 561 (5 Cir. 1958); *Majestic Co. v. Orpheum Circuit*, 21 F.2d 720 (8 Cir. 1927); *In Re Chas. K. Horton, supra; Chichester v. Polikowsky*, 231 F.2d 183 (9 Cir. 1955); *In Re Penn Central Securities Litigation*, 335 F. Supp. 1026 (E.D. Pa. 1971); *Moline Properties v. Commissioner of Int. Rev.*, 319 U.S. 436, 63 S. Ct. 1132, 87 L. Ed. 1499 (1943).

But perhaps most important with reference to the instant case are the frequent judicial statements that a mere showing that the corporate form is adopted in good faith to facilitate a particular business purpose, will justify the non-application of the *alter ego* doctrine. See *e.g.*, *Majestic*

Co. v. Orpheum Circuit, supra, at p. 725; *Moline Properties, Inc. v. Commissioner of Int. Rev., supra,* at p. 439. In *Moline,* the petitioner corporation was formed as a security device in connection with the ownership of real estate and the principal shareholder urged that the *alter ego* doctrine be applied so that he would be taxed individually on gain from the sale of some of the real estate as opposed to taxing the corporation. In upholding the validity of the corporate form, the court reasoned in terms particularly apt for the present purposes:

> "The doctrine of corporation entity fills a useful purpose in business life. Whether the purpose be to gain an advantage under the law of the state of incorporation or to avoid or to comply with the demands of creditors or to serve the creator's personal or undisclosed convenience, so long as that purpose is the equivalent of business activity or is followed by the carrying on of business by the corporation, the corporation remains a separate taxable entity." 319 U.S. at 438-439.

Where it is shown then that the corporation is deliberately adopted to secure its advantages in the service of legitimate business purpose and that the corporation functions independently to that end, it will be treated as a separate "legal person." This is to be distinguished from the situation where the affairs of the corporation are so closely intertwined with the affairs of the dominant stockholders that it is no more than his "corporate pocket" or where the so-called business purpose for the organization of the corporation is to defraud creditors by funnelling personal assets to which the creditors are entitled through the shield of the corporate entity. See *e.g., Hudson v. Wylie,* 224 F.2d 435 (9 Cir. 1957), *cert. den.,* 355 U.S. 828, 78 S. Ct. 39, 2 L. Ed. 2d 241 (1957). In this latter situation, the corporate entity is asserted as a means of fraud. But *even where fraud is alleged,* the fraud must be proved beyond mere

suspicious circumstances or the granting of valuable privileges to the coroporation. See 1 Fletcher *Cyclopedia Corporations,* §44, Permanent Edition (1933).

Courts have, on occasion, been asked to determine whether to hold the corporation responsible by applying the *alter ego* doctrine in the context of a *specific showing that the corporation was formed for tax purposes.* In *Zubik v. Zubik, supra,* suit was brought for damages to property when several barges owned by the appellant corporation broke from their moorings. On appeal was a determination that, because of the close relationship between the affairs of the Zubik corporation, a family held corporation, and Charles Zubik, Sr., the individual would be held personally liable. The reviewing court reversed the decree imposing liability on Zubik, Sr., despite certain informalities in the observance of corporate procedure, ruling that there was no evidence that funds oscillated at will between Zubik, Sr. and the corporation. The corporation, it was specifically found, was required for tax purposes. Zubik, Sr. paid for and gave shares of stock to his family and the children served as officers of the corporation. There were corporate meetings although no minutes were produced. On this and other evidence, the Court concluded, in effect, that so long as there is separate justification, unrelated to fraud or injustice for conducting personal affairs through a family corporation, the argument for ignoring the corporate entity must fail.

Similarly in *Plumbers & Fitters, Local 761 v. Matt J. Zaich Construction Co.,* 418 F.2d 1054 (9 Cir. 1969), the Court refused to pierce the corporate veil where plaintiff showed only that the corporation in question had been formed solely for tax purposes, stating the rule which must guide the determination of the issues raised on appeal by the Company:

> "The threshold question of whether piercing would be proper for the purpose intended is rarely articulated with any clarity. In principle, however, the disregarding of the corporate form of business should not rest on the manner of doing business in general but should rest on the effect that the manner of doing business has on the particular transaction involved . . . Generally speaking, *the doctrine is designed to prevent a person from doing injury and then escaping responsibility by hiding behind a corporate shield.* 418 F.2d at p. 1058 [Emphasis added]

It is clear from the above discussion that absent a significant showing, by a *preponderance of the evidence,* that the Company was *specifically formed* to avoid the liability which ICC seeks to attach to it and that the corporation operated in disregard of established corporate procedures, the *alter ego* doctrine cannot be applied. It is likewise clear from the foregoing that the Company is entitled to every reasonable presumption in its favor.

A careful reading of the June 30, 1975 transcript must reveal that ICC fell far short of carrying that burden of proof.

ICC could not refute the testimony of the Company's acountant, Alan Bloom, that the conceptualization for the Company as an estate planning device took place no later than early 1967 (994a-12 to 995a-23). In short, the purpose of the formation of the corporation was to freeze the value of Vesco's ICC stock holdings at the time of transfer, and provide that any future appreciation would inure to the benefit of the Vesco children, and pass to them free of any estate tax. Defendant's Exhibit A (1275a to 1282a) reinforces such testimony as well. ICC contends, however, that the timing of the Company's formation is somehow suspect, even sinister.

Despite lengthy testimony by Mr. Bloom, which explained the hiatus between the idea for the Company and its implementation in terms of the rise and fall of ICC's stock value (1005a-6 to 1008a-25), ICC convinced the Court that in 1972, Vesco, *certain* that the Securities Exchange Commission was about to descend upon him, secreted all his assets in the Company.

But Harry Sears, ICC's witness testified that the early part of the SEC investigation centered around not Vesco so much as ICC itself (968a-20 to 969a-2). And Bloom testified that the plan was reactivated in 1971 (1009a-12) (not 1972), prior to the period covered by Sears' testimony. Exhibits submitted, particularly the first Internal Revenue ruling request (1283a to 1288a), clearly antedate the time about which Sears was called to testify, and thus clearly undercut ICC's attempt to prove that the creation of the Company was not motivated by legitimate tax considerations.

Moreover, Sears testified that Vesco was optimistic of prevailing before the SEC (967a-13 to 968a-18), and that Vesco had received an opinion from Hogan & Hartson, eminent Securities Exchange Commission practitioners, that the SEC did not have jurisdiction over the issues being investigated.

ICC also produced as witnesses Elmer Sticco (925a to 950a) and Leonard Polisar (977a to 987a), both of whom testified that in late 1972, or early 1973, Robert L. Vesco entered into negotiations with third parties purportedly on behalf of the Company. But why should he not negotiate for the Company? He was a stockholder and an officer. Obviously, such representation of a corporate entity cannot be evidence that the corporation is a sham unless these are special rules for Robert L. Vesco and his family.

At the time of the negotiations referred to above, the Securities Exchange Commission's action against ICC and others was pending. The market value of the stock of ICC was extremely low and only Robert L. Vesco's preferred stock of Vesco & Co. had any value. And, a review of plaintiff's Exhibit 14 (1168a to 1174a), the minutes of the February 11, 1973 meeting, indicate appropriate corporate action confirming Robert L. Vesco's negotiations on behalf of the corporation.

ICC also points to the guarantee by Vesco & Co. of a loan to Robert L. Vesco (1192a). Exhibit P-14 referred to above explains that transaction. In view of the low value of the ICC stock and the consideration received for the guarantee and pledge, from Vesco & Co.'s point of view, the transaction made sound business sense.

ICC, in its arguments before the court below, emphasized the close personal relationship between Vesco and the other officers and directors of the Company, a fact which the Company does not dispute. Virtually every closely held corporation enjoys close personal relationships among its principals. But such fact could scarcely militate against a valid corporate entity, existing for a valid purpose. Nevertheless, the court's opinion reflects such "sinister" organization.

ICC argued to the court Vesco's substantial ownership of Company stock. But *Delta Theatres v. Paramount Pictures, supra; Majestic Co. v. Orpheum Circuit, supra; In Re Chas. K. Horton Co., supra; Chichester v. Polikowsky, supra,* find even sole ownership insufficient to establish *alter ego.* The Court, however, finds this as a fact as well (1080a-7 to 12), obviously imparting to it some significance.

With 20-20 hindsight, ICC and the court look back upon what has transpired since 1973 to prove a fraud in

1972. But Robert Vesco was not a "fugitive from justice" in April (when the first IRS rulings were received) or July, 1972; nor had SEC even commenced its action against him.

The Company respectfully submits that ICC totally failed to overcome the presumption of validity to which every corporation is entitled. It waged a campaign of innuendo and insinuation based both upon such hindsight and upon the notoriety of Vesco. The Court's finding upon such skimpy evidence, and in the face of all the Company's testimony to the contrary, must be reversed.

Point V

Even if other Company assets are seized, stock owned beneficially by Vesco children should remain their property.

A total of 46,380 shares of ICC common stock, which was exchanged for common stock in the Company, had been beneficially owned by the Vesco children since 1966, many years prior to the period in which the causes of action against Vesco are alleged to have accrued.

Such securities, according to the testimony of Alan Bloom at the June 30, 1975 *alter ego* hearing (1029a-15 to 1030a-13) and ICC's stipulations at that time as well as its Exhibit P-3 (1123a to 1127a), have been owned uninterruptedly on the children's behalf from that period until today. This fact is completely unchallenged.

Its history, as outlined to the court below by counsel for the Company (1074a to 1076a), was as follows:

> "Prior to December 19, 1966, Robert L. Vesco was custodian for each of his four children for 100 shares each of the stock of Captive Seal Corporation represented by Certificates No. C-39 through C-42. On

> December 19, 1966, Captive Seal Corporation merged into ICC of New Jersey and the children became the beneficial owners of 773 shares each of that corporation's common stock represented by Certificates No. 72 through 75. Also, on December 19, 1966, ICC of New Jersey merged into ICC of Florida which was formerly known as Cryogenics, Inc. Each of the Vesco children became a beneficial owner of the 11,595 shares of that corporation's common stock. ICC of Florida is the plaintiff in the within action" (1076a-1 to 11).

No evidence whatever was submitted to indicate, or even suggest, that these shares were fraudulently conveyed to the children; yet the court below ordered that all of the Company's securities, including the children's shares, be seized to satisfy ICC's judgment against Vesco.

If a court pierces the corporate shield on an *alter ego* theory, the corporation's assets return to *status quo ante*. The language frequently utilized where there is a finding of *alter ego*, provides that "the corporate form may be disregarded and *the substance of the action* dealt with in the interest of justice." *Bangor Punta Operations v. Bangor & Aroostook R. Co.*, 417 U.S. 703, 94 S. Ct. 2578, 41 L. Ed. 2d 418 (1974); *Plumbers & Fitters, Local 761 v. Matt J. Zaich Construction Co.*, 418 F.2d 1054, 1058 (9 Cir. 1969).

ICC, in the case *sub judice* sought alternatively to reach the assets of the Company on a fraudulent conveyance theory. Although the court below, having made an *alter ego* finding, declined to deal with that issue, had it done so, the securities would still, as a matter of law, revert to the Vesco children.

37 *C.J.S., Fraudulent Conveyances*, §307 p. 1138, states:

> "Since . . . a fraudulent conveyance is void as to creditors, they may generally pursue legal process

> against the subject of the conveyance. *The title,* for the purpose of enabling creditors to enforce their debts against the property conveyed, *still remains in the grantor, just as though the conveyance had not been made.* A direct action to set aside the fraudulent conveyance is not required" (emphasis added).

See also, *Empire Lighting Fixture Co. v. Practical Lighting Fixture Co.,* 20 F.2d 295 (2 Cir. 1927). In case of stock, creditors may treat the conveyance as a nullity, without the necessity of procuring a decree in equity. 37 *C.J.S.* at 1138.

The rule is substantially the same as stated in the Bankruptcy Act §70(e) (11 *U.S.C.* §110). The trustee in bankruptcy may simply set aside a transfer proved fraudulent. *Feldman v. Chase Manhattan Bank,* N.A., 368 F. Supp. 1327 (S.D.N.Y. 1974), *rev'd on other grounds,* 511 F.2d 468 (2 Cir. 1974).

ICC is not entitled to be placed in a better position than it would have occupied had the Company never been formed.

The Company respectfully submits that, even assuming, *arguendo,* that this court finds ICC's *alter ego* theory to have been proved by a preponderance of the evidence, the 46,380 shares of Company stock must be returned to their original owners, the Vesco children for whom their mother presently holds them in trust, and cannot, under any circumstances, be seized or cancelled herein.

CONCLUSION

For the reasons expressed herein and upon the evidences adduced heretofore, it is respectfully submitted that this Court, on appeal, should:

1. Reverse the determination below on the ground of inadequacy of the evidence presented in light of applicable law; or

2. Vacate the judgment below, with directions to the trial court to stay any further proceedings in this connection until: (a) full and final judgments are rendered on the underlying claims as against Vesco and other alleged joint tort feasors; and (b) plenary hearings are held on all of the issues sought to be raised by defendant Vesco & Co., Inc., both procedural and substantive; and in any event,

3. Modify the judgment below insofar as it purports to permit and direct seizure of stock owned beneficially by Vesco children.

Respectfully submitted,

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Defendant-Appellant,
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By: /s/ James J. Shrager
JAMES J. SHRAGER
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Dated: December 17, 1975.

JAMES J. SHRAGER
SUSAN I. LITTMAN
On the Brief

IN THE

~~Supreme Court of New Jersey~~
UNITED STATES COURT OF APPEALS
For The Second Circuit
Docket No.75-7548

PROOF OF SERVICE FORM
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International Controls Corp.,

Plaintiff-Appellee,

vs.

Robert J. Vesco, et al.,

Defendants,

and

Vesco & Co., Inc.,

Defendant-Appellant

STATE OF NEW JERSEY)
:ss.
COUNTY OF MIDDLESEX)

PROOF OF SERVICE

I, JAMES B. RATTIGAN, of full age, being duly sworn according to law upon my oath, depose and say:

1. I am the Vice President of New Jersey Appellate Printing Co., Inc., a New Jersey corporation, the principal place of business of which is located at 399 Pearl Street, Woodbridge, New Jersey

2. On the 17th day of Dec. 1975, I hand delivered by messenger ~~placed in the Post Office at Woodbridge, New Jersey~~, a package containing

2 copies each of printed Brief, Appendix Volume 1 and Volume 11 and 1 Volume Exhibits

~~first class mail~~, addressed:

Shea, Gould, Climenko, Kramer & Casey, Esqs.
330 Madison Avenue
New York, New York 10017
Att: Daniel L. Carroll, Esq.

Sworn and subscribed to
before me this 17th day
of Dec. 1975.

Ronald D. Anzivino

RONALD D. ANZIVINO
NOTARY PUBLIC OF NEW JERSEY
My Commission Expires Feb. 9, 1976

James B. Rattigan

JAMES B. RATTIGAN